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UNITED STATES
POSTAL SERVICE

July 23, 2012

Shoshana M. Grove
Secretary
Postal Regulatory Commission
901 New York Avenue, NW, Suite 200
Washington, DC 20268-0001

Re: Docket Nos. R2011-3 and MC2011-19

Pursuant to Order No. 694 in Docket Nos. R2011-3 and MC2011-19, the Postal Service presents its Data Collection Report on the Discover Financial Services, Inc.'s Negotiated Service Agreement with the United States Postal Service.

Sincerely,

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DISCOVER FINANCIAL SERVICES NEGOTIATED SERVICE AGREEMENT
DATA COLLECTION REPORT
(APRIL 1, 2011 – MARCH 31, 2012)

INTRODUCTION

Pursuant to Order No. 694 in Docket Nos. R2011-3 and MC2011-19, the Postal Service presents its Data Collection Report ("DCR") on the Discover Financial Services, Inc.'s ("DFS") Negotiated Service Agreement ("NSA") with the United States Postal Service ("Postal Service").

COMMISSION REQUESTED DATA

1. **DFS's volumes entered by qualifying price category for the just ended contract year.**

   See DCR Appendix A, page 1.

2. **DFS's postage paid by qualifying price category for the just ended contract year.**

   See DCR Appendix A, page 1.

3. **The adjusted threshold used to establish DFS' eligibility for rebates and payment of fines, and the calculations underlying the threshold's determination.**

   See DCR Appendix A, page 2.

   The revenue threshold will be adjusted upward by 65 cents for every one dollar decline in DFS' eligible First Class Mail ("FCM") postage, which means DFS must spend an additional $1.65 on Standard Mail to offset each dollar decline in postage from FCM.

   DFS' FCM volume did not decline in Year 1; therefore, the postage threshold was not adjusted.

4. **The index used to establish DFS's average price increase, and the calculations underlying the index's determination.**

   See DCR Appendix A, page 3.

   The Postal Service used the Laspeyres Index to establish DFS' average price increase. This index uses the weighted volume distribution by price category (within the class of mail) for the year preceding contract Year 1, and then uses the published prices for those categories to examine price change.

Specifically, to calculate the index for FCM, the Postal Service compared the published price for each rate category at the start of Year 1 (35.5 cents) to the published price for each rate category at the end of the Year 1 (37.2 cents) for an increase of 1.7 cents per piece, (index of 104.7).

To calculate the index for Standard Mail, the Postal Service compared the published price for each rate category at the start of the Year 1 (20.0 cents) compared to the published price for each rate category at the end of the Year 1 (20.9 cents) for an increase of 0.9 cents per piece (index of 104.6).

5. **The rebate paid or penalty paid by DFS (if any) and the calculations underlying their determination.**

See DCR Appendix A, page 2.

DFS earned a total rebate of $5.6 M on the letter-size IMb FCM and Standard Mail volume since it exceeded the revenue threshold for Year 1.

The number of FCM pieces eligible for the rebate (less those pieces that received the Mobile Barcode rebate) is 200,235,004 pieces. The rebate is calculated on 75 percent (75% of 1.7 cents = 1.28 cents) of the price increase (see Laspeyres Index). The rebate on the FCM volume was $2,571,996 (200,235,004 X 0.0128).

The number of Standard Mail pieces eligible for the rebate (less those pieces that received the Mobile Barcode rebate) is 893,490,495. The rebate is calculated on 37.5 percent of the price increase (37.5% of 0.9 cents = 0.34 cents). The rebate on the Standard Mail volume was $3,051,958 (893,490,495 X 0.0034).

6. **A list of all subsidiaries and affiliates mailing eligible mailpieces during the contract year as well as lists of all mergers and acquisitions and sales and closures of entities or divisions occurring during the contract year; and volumes associated with such enterprises for that contract year.**

None of DFS' subsidiaries and/or affiliates mailed eligible mailpieces during Year 1 of the agreement. There were also no mergers, acquisitions, sales or closures of entities or divisions during Year 1 of the agreement.

7. **The methodology and calculation used to determine the increase or decrease in net contribution to the Postal Service as a result of the agreement for the just ended contract year; including a narrative explanation of the methodology used.**

See DCR Appendix A, page 4.

In Appendix F, page 1 of Notice of the United States Postal Service of Filing of Contract and Supporting Data and Request to Add Discover Financial Services Negotiated Service Agreement to the Market-Dominant Product List, the Postal Service provided volume projections for FCM and Standard Mail letter-size mailpieces. Specifically, these projections, which were based on historical trends, represented volume data over a three-year period in the absence of an incentive offering and NSA.

In DCR Appendix A, page 4, the first column of data contains the Year 1 volume projections. Standard Mail letter-size volume data is presented with a low and high estimate. In order to calculate the net contribution increase to the Postal Service, volume projections (both FCM letter-size and Standard Mail low and high estimates) are subtracted from the actual volumes in Year 1. The incremental volume recorded in the third column on page 4 of DCR Appendix A represents the difference between the actual volumes in Year 1 (with an incentive offering) and the Year 1 projected volumes (without an incentive offering).

To calculate the net value of the incremental volume, the Postal Service begins with the average weighted revenue per piece for each mail category (as stated in DCR Appendix A, page 1), minus the average weighted unit cost (DCR Appendix A, page 1) to determine the average weighted unit contribution. The average weighted unit contribution is multiplied by the respective incremental volume to calculate the new total contribution. Then, the total earned rebates paid (DCR Appendix A, page 2) are subtracted from the incremental value. Using the low and high estimates, the net contribution resulted in a $24.8 million to $26.8 million, respectively. The complete calculations are provided in the attached DCR Appendix A, page 4.

8. The annual (contract year) actual mailer-specific costs, volumes, and revenues.

See DCR Appendix A, page 1.

9. A detailed discussion of how the Postal Service believes DFS's own-price elasticities differ from the average elasticities of work shared First-Class Mail and Standard Regular Mail.

The Postal Service can not quantify how DFS' own-price elasticities differ from the average elasticities of work shared First-Class Mail and Standard Regular Mail. The Postal Service does not measure how elasticities differ by customer. Obviously, the large groupings for which we have measures of elasticity are a composite of many customers; each of which may react to price changes differently.